EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF THE UNITED STATES TRADE REPRESENTATIVE
WASHINGTON, D.C. 20508

OCT 9 2001

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The Honorable Sheila Kuehl
California State Senate
Sacramento, CA 95814

Dear Senator Kuehl

Thank you for your letter outlining your concerns regarding investment provisions of the North American Free Trade Agreement (NAFTA). Ambassador Zoellick requested that I respond and provide some guidance as to what to expect with respect to these issues and the proposed Free Trade Area of the Americas (FTAA).

You raise a concern that the investment provisions might allow foreign investors to challenge legitimate regulatory actions. This is a matter that we take very seriously. The investment protections codified in NAFTA and other U.S. investment treaties are designed to protect investors against arbitrary, discriminatory or expropriatory government action. At the same time, Article 1114 (1) explicitly preserves the right of NAFTA countries to maintain or enforce environmental regulations that are consistent with these principles and deemed necessary to ensure that investment activity within its borders is undertaken in a manner sensitive to environmental concerns.

It is important to recognize that no arbitral tribunal has found a U.S. labor or environmental regulation to be inconsistent with NAFTA or any other investment agreement. Furthermore, the investor-state arbitration process cannot force the federal or state governments to revoke environmental, labor or any other type of laws or regulations. Arbitral tribunals may award compensation to an injured investor but have no authority to strike down a government measure.

Take, for example, the *Metalclad* case against Mexico. In that case, the arbitral tribunal found that a local government expropriated a U.S. investor's property when it issued a decree designating the area on which the investor's facility was built as an ecological zone for the protection of a rare cactus. This finding was upheld by a Canadian court. The protection in NAFTA against uncompensated expropriations is not new. Such principles are found in customary international law and the United States Constitution.

We continue to believe that the investor-state dispute settlement mechanism and the underlying investment provisions are an important part of our investment agreements. It is an extremely valuable tool for our own investors to ensure that they have access to a neutral forum to litigate disputes with governments which might not have a fully developed and fair judicial system. However, we have learned from experience that greater clarity is necessary to ensure that NAFTA is interpreted correctly.

We are taking concrete steps to clarify the obligations assumed in our investment agreements and specify in greater detail how the mechanism should operate.

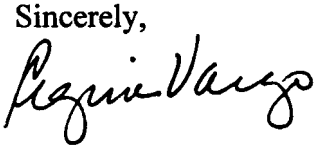
I call your attention to the fact that we recently agreed with our NAFTA partners to a clarification of certain provisions of the investment chapter in NAFTA (enclosed). The interpretation that we have adopted will make the investor-state dispute settlement process more transparent and spells out how the "minimum standard of treatment" required by NAFTA should be interpreted. We are continuing to explore ways to ensure that the dispute settlement process operates fairly and that our obligations are not misinterpreted by an arbitral tribunal. This process will help shape our investment proposals in the FTAA and other future investment agreements.

The thrust of the questions you pose appears driven by public commentary on the pending *Methanex* case. It is important to emphasize that no conclusions can be drawn from this case since the arbitration is not yet completed. I would note, however, that the mere fact that an allegation has been made is not a basis for asserting that the investor protections are flawed. Spurious claims are often made, even in domestic U.S. courts. If a claim is found to be without merit after the arguments have been presented, it should be rejected.

Investment provisions are among the many topics being considered within the FTAA negotiations. We maintain close contact with a range of stakeholder groups on all aspects of the FTAA negotiations and regularly solicit public input into the process. In early July, the draft negotiating text of the FTAA, including the chapter on investment, was released to the public and a Federal Register notice soliciting public comment on the draft text was published. Both the draft negotiating text and the Federal Register notice can be accessed through our web-site at www.ustr.gov.

Thank you for your letter and your interest in this subject. We appreciate you bringing your particular concerns to our attention and look forward to working with you and others on this and other important trade issues.

Sincerely,



Regina Vargo
Assistant U.S. Trade Representative
for the Americas

Enclosure

Having reviewed the operation of proceedings conducted under Chapter Eleven of the North American Free Trade Agreement, the Free Trade Commission hereby adopts the following interpretations of Chapter Eleven in order to clarify and reaffirm the meaning of certain of its provisions:

A **Access to documents**

1 Nothing in the NAFTA imposes a general duty of confidentiality on the disputing parties to a Chapter Eleven arbitration, and, subject to the application of Article 1137(4), nothing in the NAFTA precludes the Parties from providing public access to documents submitted to, or issued by, a Chapter Eleven tribunal.

2. In the application of the foregoing:

(a) In accordance with Article 1120(2), the NAFTA Parties agree that nothing in the relevant arbitral rules imposes a general duty of confidentiality or precludes the Parties from providing public access to documents submitted to, or issued by, Chapter Eleven tribunals, apart from the limited specific exceptions set forth expressly in those rules.

(b) Each Party agrees to make available to the public in a timely manner all documents submitted to, or issued by, a Chapter Eleven tribunal, subject to redaction of:

(i) confidential business information;

information which is privileged or otherwise protected from disclosure under the Party's domestic law; and

information which the Party must withhold pursuant to the relevant arbitral rules, as applied.

(c) The Parties reaffirm that disputing parties may disclose to other persons in connection with the arbitral proceedings such unredacted documents as they consider necessary for the preparation of their cases, but they shall ensure that those persons protect the confidential information in such documents.

(d) The Parties further reaffirm that the Governments of Canada, the United Mexican States and the United States of America may share with officials of their respective federal, state or provincial governments all relevant documents in the course of dispute settlement under Chapter Eleven of NAFTA, including confidential information.

3. The Parties confirm that nothing in this interpretation shall be construed to require any Party to furnish or allow access to information that it may withhold in accordance with Articles 2102 or 2105.

B. Minimum Standard of Treatment in Accordance with International Law

Article 1105(1) prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investments of investors of another Party.

2. The concepts of "fair and equitable treatment" and "full protection and security" do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens.

3. A determination that there has been a breach of another provision of the NAFTA, or of a separate international agreement, does not establish that there has been a breach of Article 1105(1).

Closing Provision

The adoption by the Free Trade Commission of this or any future interpretation shall not be construed as indicating an absence of agreement among the NAFTA Parties about other matters of interpretation of the Agreement.

Done in triplicate at Washington, D.C., on the 31st day of July, 2001, in the English, French and Spanish languages, each text being equally authentic.

For the Government of the United States of America	**For the Government of the United Mexican States**	**For the Government of Canada**
Robert B. Zoellick United States Trade Representative	Luis Ernesto Derbez Bautista Secretary of Economy	Pierre S. Pettigrew Minister for International Trade